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Realty Stock Review

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MARKET STRATEGY: MARKET CROSSCURRENTS SIGNAL CHOPPY INVESTMENT WATERS IN 1987

One crosscurrent is very bearish for realty stocks, the other very bullish. So far investors seem to be focusing on the bearish news without looking at the opposite tide. The currents we see:

--**Bearish:** Dividend cuts are coming faster among many REITs and other realty stocks. It's been 18 months since two trusts managed by Consolidated Capital Cos. cut dividends in Aug. 1985, signaling the start of a down cycle. In the past year our tally finds three REITs have omitted regular dividends (**Americana Hotels, ConCap Realty and First Continental REIT**) and 15 other large REITs have now cut payout, as follows:

Trust	Jan. '86	Latest	% Chg.
California REIT..	\$1.28	\$0.60	-53%
CleveTrust Rlty..	2.00	1.40	-30
Eastgroup Props..	4.17	2.90	-31
INVG Mtg.Secs....	6.80	2.00	-71
L&N Housing.....	2.65	1.96	-26
Lomas & Net.Mtg..	2.61	2.44	- 7
Mtg. Invest. Plus	1.00	0.80	-20
Mellon Partic.Mtg	1.00	0.96	- 4
Prop. Trust Amer.	1.20	0.80	-33
Realty South.....	2.31	1.60	-31
Storage Equities.	1.92	1.40	-27
Travelers REIT...	1.04	0.92	-12
Travelers Rl.Inc.	1.60	1.40	-13
Webb Invest.Prop.	0.90	0.45	-50
Wells Fargo Mtg..	2.80	2.00	-29

Cuts most frequently stem from:

(1) Troubled investments, generally in the Oil Patch, which played major roles in **Americana, California REIT, ConCap Realty, CleveTrust, First Continental, Property Trust of America**, the two **Travelers REITs**, and **Wells Fargo**.

(2) Lower reinvestment rates, generally on rollover of mortgages, especially hurting **Eastgroup, L&N Housing, Lomas & Nettleton Mtg., Mellon, Mortgage Investments Plus**, and **Realty South**.

--**Bullish:** A continuing supply of big money, mostly offshore, is willing to step up and pay good prices for realty stocks. Examples:

In November Virginia based **NVHomes L.P.** won control of **Ryan Homes**, an established Pittsburgh based builder, in a \$390 mil. deal cut at \$48/sh.

Benequity Holdings, an MLP, this week agreed to let Australian based **Renouf Corp.** International either to tender at \$31 for all 5.7 mil. BH shs. or cease efforts to take over BH. **Renouf** is an Australian and New Zealand merchant banking and property company. The potential \$178 mil. deal is at 7% premium over BH's posted \$28.98/sh. current net asset value.

Princeville Development Corp., owner of a major Hawaiian land development, agreed to let **Qintex America Ltd.**, subsidiary of a \$500 mil. Australian
(continued on page 2)

RANKING REVIEW ISSUE		REVIEWS OF STOCKS		
Market Strategy.....	1	CleveTrust Realty Invest.	6	Johnstown Amer. Cos....2
Realty Stock Averages.....	6	Consol. Capital Realty I.	4	JMB Realty Investors...6
		Hallwood Group Inc.....	2	Mortgage & Realty Tr...5
				Security Capital Corp..4

Stock charts courtesy Mansfield Stock Chart Service

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(continued from page 1)

investment company, tender for 3.3 mil. shs. (40%) at \$13.00 cash. Upon completion, PDC would sell 1.2 mil. new shs. to Qintex for \$12.50, which with 390,000 shs. owned would give it voting control. Non-tendering holders will receive special value protection notes with a maximum value of \$5.75/sh. Spinner Corp. abandoned a PDC takeover attempt. We advise tendering.

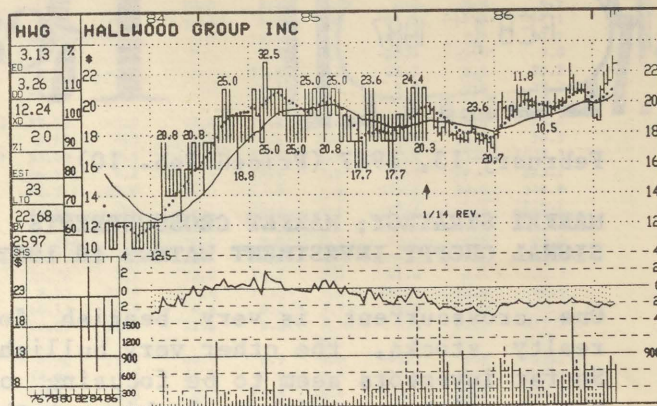
These trends can work in tandem. Any one of the dividend cutters may fall to a price low enough to attract bargain hunters. Wells Fargo Mtg. for instance posts a \$30.22/sh. current asset value as of June 1986, yet now sells at about \$22 or a 26% discount from NAV. We review this issue several stocks well situated for investors working both ends of this spectrum.

RANKING REVIEWS: THREE DIVERSIFIED COMPANIES POSITIONED FOR CONTRARIANS

Hallwood Group Inc. (\$23.75--NYSE), reconstructed from three former sick REITs, is positioning to be a speciality merchant banker for other ailing companies. Real estate is a smaller piece of the pie now. We are holding B Rank.

EPS/Dividends - B: HWG earned \$2.12 share in its July 1986 fiscal year, including 33¢ taxloss carryforward benefit, the total up 56%. HWG paid \$1.12/sh. dividend on the common, unchanged. All numbers are adjusted for a 1-for-14 reverse split effected to win broader investment support. HWG earned 18¢ including 4¢ taxlosses in the Oct. qtr., down 38%.

Assets and Operations: HWG's \$27.2 mil. revenues in 1986 rose 23% and derived 48% financial services including merchant banking fees and interest on mortgages and receivables, most from property sales; 46% from real estate operations of a \$51 mil. property portfolio and gains on property sales; and 6% interest and other. Financial services generated 79% of operating income and real estate the rest. HWG operates real estate in England (9% of operating profit in 1986) and during 1986 acquired Bank Insinger Willems of Netherlands, which should contribute in 1987. HWG's principals are trying to restructure

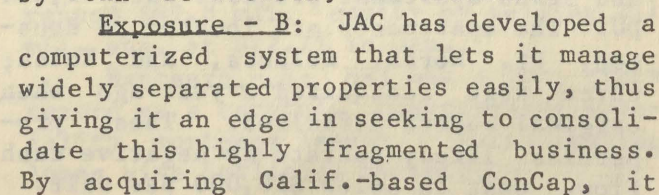


troubled companies thru discounted rights offerings (i.e., existing shareholders are given the right to buy new shares below current market). In 1985 it restructured troubled Saxon Oil Co. and last year assisted Brock Hotels in resolving its debt problems. It recently agreed to help restructure GCA Corp., troubled maker of a key component of semiconductors, and has hired a former Oklahoma banking official to seek troubled Oil Patch banks.

Financial Measures - A: HWG follows a policy of restricting leverage and \$16.9 mil. debt is 0.20 times net shareholders' equity of \$82.6 mil. or \$16.99 per share. Most debt is property related. Liquidity is high with \$14.7 mil. cash (\$3.20 sh.) on hand. Officers own 12%.

Exposure - B: HWG has followed an unorthodox game plan in recycling funds from real estate assets into merchant banking. Goal is to produce earnings to use \$2.36/sh. taxloss carryforwards. Limitation is the complexity and attendant time required to complete major merchant banking deals. We remain constructive and include HWG in our financial services group.

Johnstown American Cos. (\$3.63--ASE) holds C Rank. JAC has hit an earnings airpocket since acquiring the major West Coast syndicator, Consolidated Capital Equities Corp. in July 1985. JAC was one of the bigger losers in realty stocks in both 1985 and 1986 (see RSR, Jan. 9), falling 49% last year to touch 2-3/4 at one point. Now it has moved off its lows (chart) and the near-term potential for recasting the price paid for ConCap could aid book value.



ended risk that an independent ConCap would give management of its properties to another company. But ConCap also puts JAC into the ranks of major realty syndicators, where sales of new programs and profits are often determined by tax law changes and investment trends. The 1986 Tax Reform Act hurt sales of shelter-oriented limited partnerships and widely publicized troubles at two ConCap REITs hurt broker relations. But ConCap seems to be recovering with income syndications and restructured management. JAC may emerge stronger.

Consolidated Capital Realty Investors (\$4.50--NASDAQ) holds C Rank in our review, even tho we do not yet have final numbers on its Nov. 1986 fiscal year. CCPLS was 1986's biggest loser, off 71% (see RSR, Jan. 9) and traded as low as \$2.75 when it ended regular dividend payments. CCPLS was organized in 1975 as ConCap's early version of a "vulture" fund, formed to acquire semi-distressed properties of that day. It has now liquidated most properties, taking back purchase money or wrap mortgages for many.

EPS/Dividends - C: CCPLS earned 30¢ from operations in the 9 mon. thru Aug., down 12%. In addition it netted 19¢ from property sales and note revaluations, down from \$1.40/sh. Total income was thus 49¢, all of which was distributed. About 60% of 1986 payout is expected to be treated as capital gain.

Property sales: CCPLS continues to sell properties and in Sept. sold three properties, all for gains: a 1,682-DU Houston apartment sold for \$26.5 mil. or \$15,755/DU; a 300 DU Dallas apartment sold for \$4.4 mil. or \$14,667/DU; and a Utah shopping center for \$2.7 mil. or \$27.62/SF. CCPLS received 3.6% cash in the total \$33.6 mil. transactions, taking back \$17.3 mil. notes and mortgages with buyers assuming \$15 mil. debt.

The sales leave CCPLS with a 218,000 SF Pocatello, ID shopping center and seven apartment projects with 1,864 DU. The apartments are located in Houston, Ft. Worth, Atlanta, and Tulsa; three were reacquired a year ago when original buyers defaulted. These properties likely operate at negative cash flow. Cost is below \$16,000 per unit.

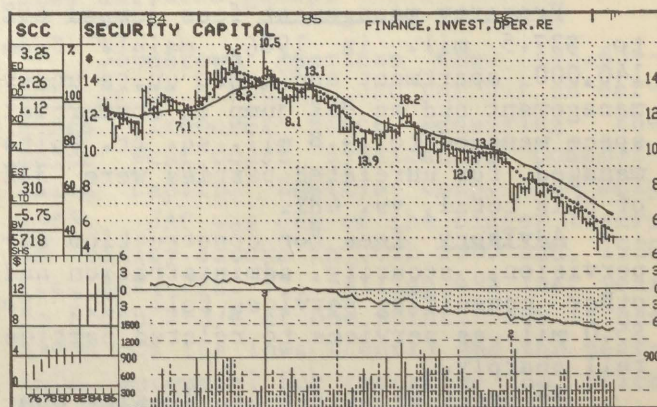
Notes receivable sales: Since CCPLS frequently sells properties by taking back wrap-around and other mortgages, it has built a \$101.1 mil. portfolio of notes and contracts receivable adjusted for the recent sales. After \$43 mil. related payables, CCPLS has \$58.1 mil. net equity in these notes, which is further haircut by \$35 mil. deferred gains and unamortized discount (\$5.87/sh.) under accounting treatment. Since this net equity is not readily liquid, CCPLS borrowed \$11.75 mil. from First Union Real Estate in March 1986 at 15.5%, securing the loan by its net equity in three sold properties.

Financial Measures - C: Property related debt of \$28.5 mil. is 0.9 times \$31.7 mil. net equity. Net equity plus depreciation equals \$8.94/sh. not including \$5.87/sh. deferred gains. Liquidity is tight.

Exposure - C: With most remaining properties in Oil Patch areas, CCPLS is a recovery candidate. Management historically has been agile in tough markets.

Security Capital Corp. (\$5.50--ASE) falls to C Rank as earnings vanished under onslaught of the Houston real estate market. Assets under management increased and liquidity held up well. **EPS/Dividends - C:** SCC lost \$1.52/sh. in its Sept. 1986 FY, vs. \$1.72/sh. diluted gain. The loss broke a string of annual gains the past five years for this former REIT. The loss resulted because SCC set aside \$3.95/sh. (\$23.3 mil.) as loss on loans for its Houston S&L subsidiary. SCC has been paying 20¢ annually.

Assets and Operations: SCC is emerging as a financial services company with these major operations:



Savings & loan: SCC owns Ben Franklin Savings of Houston, which operates 18 branches in Houston, Dallas and Ft. Worth and has \$2.1 bil. assets; liabilities are match-funded with mortgage and other assets, to minimize interest risks. However rates on short-term assets tended to fall faster than on related liabilities during 1986, shrinking the positive interest spread to 2.35% from 2.74% in 1985. In response to regulatory capital requirements and an increase in scheduled items (non-earning loans and foreclosures) to 10.0% of specified assets, Ben Franklin deferred making new commitments in 1986, which further reduced income. Regulatory capital of \$76 mil. at year-end exceeds requirements of \$70.3 mil.

Mortgage banking and brokerage: Foster Mortgage, a mortgage banker, services \$2.6 bil. mortgages and originated \$746 mil. mortgages in 1986, up 45%. Expenses of delinquencies and foreclosures hurt earnings however.

Real estate development: SCC develops real estate both directly and thru Ben Franklin. At year-end Ben Franklin had invested \$96.6 mil. in two major land projects, of 1,174 acres near Austin zoned for mixed use, and of 357 acres in Houston.

Real estate management for pension plans: Thru wholly owned Security Capital Real Estate, SCC manages \$1.12 bil. properties for pension plans and partnerships. Fee income is rising and generated \$3.2 mil. operating profit in 1986, SCC's best performing unit.

Finances: SCC's balance sheet consolidates its S&L sub so total liabilities of \$2.25 bil. including \$1.64 bil. S&L deposit liabilities, are 38.1 times book equity, or \$10.43/sh. All debt, excluding HLBB advances, of \$284 mil. is 4.8 times book equity. Book equity includes \$104 mil. intangibles arising from the Ben Franklin acquisition.

Exposure: SCC's moves to reduce interest rate risk and maximize interest and fee income have been overwhelmed for now by magnitude of the Texas recession. Outcome for the Houston S&L holding is uncertain. Management however has built a significant company on the base of an older REIT and we think they can come back again.

RANKING REVIEWS: CLEVETRUST REALTY FALLS IN RANK; MORTGAGE & REALTY AND JMB HOLD

Mortgage & Realty Trust (\$21.38--NYSE) holds A Rank. EPS/Dividends - A: MRT earned \$2.13 sh. from operations in its Sept. 1986 fiscal year, vs. \$1.78. The 1986 total included 49¢ additional interest resulting from prepayment of participating loans and 10¢ property sale gains; the prior year had only 5¢ sale gains. Operating income thus fell 11% to \$1.54. Operating income of 41¢ in the Dec. qtr. was up 2.5% from the Sept. qtr. and up 5% from 1985; the Dec. qtr. also included 1¢ additional interest vs. 33¢ from this source and sale gains the year before. MRT is paying \$1.88 annually, up 4%, and in 1986 paid another 31¢ extra from additional interest.

Additional interest income: Since MRT began making participating mortgages (i.e., loans in which MRT shares in rental increases) several years ago, it has received periodic payments of additional interest as these loans were repaid, mostly because of lower rates.

Assets: MRT held \$356 mil. invested assets at Dec. 31, up 36% in a year, divided 94.7% earning mortgages, 1.5% property investment, and 3.7% nonearning loans and foreclosures (a percentage down from 5.5% a year ago and level with long-term averages). Mortgages are 48% standing loans, 20% construction/development, 9.5% long-term amortizing; and 18.7% participating and participating/construction loans. This latter type has risen over recent years and gave rise to the 1986 kicker income. MRT has moved into participating mortgages the last three years and had \$144 mil. unfunded commitments at Dec. 31.

Financial Measures - A: Debt of \$217 mil. at Dec. 31 is 1.6 times equity of \$135.2 mil. or \$16.46/sh. Debt is 59% short-term floating rate (commercial paper and bank); 9% medium-term revolving credit; and 32% long-term fixed rate, which matches well with asset maturity. Liquidity is good and MRT raised \$47.8 mil. equity by selling 2.1 mil. shs. at \$22.75 in Jan.

Exposure - A: MRT has a long track record as a careful, conservative speciality mortgage lender. Participating loans give inflation protection.

CleveTrust Realty Investors falls to C Rank. This is a close call but continued drag in property operations nudges CTRIS below B Rank.

EPS/Dividends - B: CTRIS' Sept. 1986 earnings and net cash flow are again obscured by non-recurring or special items meriting special analysis: (1) Expenses of 35¢ for proxy contest with a dissident shareholder; and (3) 44¢ gain on sale of land previously leased by CTRIS. Putting these together shows per share results for Sept. '86 year:

	EPS	CFS
Operating income/CFS..	\$0.03	\$0.61
Proxy expense.....	(0.35)	(0.35)
Operating EPS/CFS.	(0.32)	0.26
Property sale gains...	0.44	0.44
Total EPS/CFS.....	\$0.12	\$0.70

The proxy contest resulted after shareholder Robert Goodman protested CTRIS' repurchase, in Oct. 1985, of 847,209 sh. from the former largest shareholder, Merchant Navy Pension Plan of England, for \$19/sh., paid half cash, half in 12% notes. The note portion was retired in Oct. 1986.

CTRIS earned 6¢ from operations in the Dec. qtr., including 1.7¢ from property sales. EPS also benefitted from 9¢ gain on debt retirement. Dividends were cut to \$1.40/sh. during the year, which is still not covered by current cash flow.

Assets and Operations: Net invested assets of \$55.3 mil. at Sept. 30 before loss reserve are 66% direct ownership of property and 34% mortgages. Properties at cost are about 65% offices with 621,000 SF; 14% commercial including a St. Louis hotel and retail; and 20% apartments and other. Major offices are

located in Tulsa, Dallas and the Denver area, where strong competition for tenants has limited results. In Oct. CTRIS purchased ownership of a 121,000 sq. ft. Austin, Tex. shopping center on which it previously held a convertible loan, for \$7.63 mil. total cost or \$63/SF. In Oct. it also sold a non-earning Brunswick, O. shopping center at a gain.

Financial Measures - A: Debt of \$25.8 mil. is 0.7 times the \$36.5 mil. sum of shareholders' equity (\$24.95 mil. or \$12.48/sh.) and accumulated depreciation (\$11.59 mil. or \$5.80/sh.). Debt is 40% mortgages secured by property, the rest bank and other debt.

Exposure - C: At the property level, CTRIS continues exposed to weak Southwestern office markets. Property net operating margins have dropped two years running and net cash flow has fallen. CTRIS hopes to diversify holdings beyond the Oil Patch.

JMB Realty Trust remains at B Rank for its Aug. 1986 fiscal year.

EPS/Dividends - B: JMBRS netted \$1.61 from operations, down 10%, due to lower interest on mortgages sold the prior year, offset in part by higher rentals on enclosed Sycamore Mall, Iowa City, acquired June 1985. JMBRS also earned 23¢ from property dispositions, down from 66¢. Dividends totaled \$1.64.

JMBRS holds mainly land purchase leasebacks and wraparound mortgages.

Current value: JMBRS estimates current value at \$18.66/sh., up 1.7% from Aug. 1985 and 9.6% above cost-basis equity of \$17.03/sh. Value reduction of a Houston apartment leaseback and repurchase of land beneath a Las Vegas hurts.

COMPARATIVE REALTY STOCK GROUP AVERAGE 02/10/87

GROUP NUMBER & NAME	DIV	NON-DIV	TOTAL	SHARE (000)	BOOK VALUE	ANNUAL DIV	EARN ANN	LAST PRICE	-% CHANGE FROM JAN 20	FROM JAN 1	P/E RATIO	ANNUAL YIELD	% PR TO BK	RETURN ON BK	MARKET VAL.(000)
1 PROPERTY REITS	45	6	51	6452	10.87	1.10	1.14	16.06	-0.2	3.7	14.0	6.8	47.8	10.5	5698.8
2 PROP & MTG COMB REITS	21	4	25	5706	13.00	1.31	0.99	14.57	-2.3	0.8	14.7	9.0	12.1	7.6	2138.4
3 MORTGAGE REITS	16	2	18	5169	14.25	1.52	1.41	16.13	-2.9	0.1	11.5	9.4	13.1	9.9	1648.0
4 PARTICIPATING MTG REITS	12	0	12	8220	12.62	1.14	1.25	12.97	-1.6	-0.6	10.3	8.8	2.8	9.9	1425.3
5 MAJOR HOMEBUILDERS	8	4	12	16914	10.96	0.48	1.56	21.58	3.7	14.5	13.8	2.2	96.9	14.2	3594.6
6 OTHER BLDRS/DEVELOPERS	8	26	34	6100	5.42	0.19	0.50	9.47	5.1	13.9	18.8	2.0	74.9	9.3	2108.4
7 INCOME PROP BLDR/OWNR	21	11	32	6610	11.52	0.77	0.88	18.17	1.8	6.8	20.7	4.2	57.6	7.6	3863.4
8 MORTGAGE BANKER/FINANCE	13	4	17	13056	9.91	0.82	1.23	16.26	6.3	9.5	13.2	5.0	64.0	12.4	5710.7
9 DIVERSIFIED RLTY HOLDING	13	6	19	24042	14.48	0.33	1.01	19.75	2.8	11.5	19.6	1.7	36.4	7.0	15591.0
10 RLTY SVCS/SYNDICATORS	2	4	6	8188	6.60	0.04	-0.31	8.88	11.8	13.9	0.0	0.5	34.5	-4.7	390.4
11 MANUFACTURED HOUSING	4	5	9	12427	6.68	0.16	0.43	11.67	2.2	16.1	27.3	1.3	74.7	6.4	1359.2
L LIQUIDATING COMPANIES	0	1	1	5968	1.37	0.00	-1.27	2.50	-13.0	-4.8	NC	NC	82.5	NC	14.9
P PREFERRED STOCKS	1	0	1	1650	10.00	1.10	0.00	12.63	2.0	4.1	NC	NC	26.3	NC	20.8
OVERALL AVERAGE			237	9042	10.70	0.80	0.98	15.33	1.4	6.7	15.7	5.2	43.2	7.5	43564.0
DOW JONES INDUSTRIALS							118.80	2158.04	2.5	13.8	18.2	3.1			
STANDARD & POOR'S 500							14.89	275.07	2.2	13.6	18.5	3.1			
DOW JONES UTILITIES							14.91	221.50	-1.2	7.5	14.9	7.2			